

# 457(b) Plans for the 401(k) Administrator



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# Overview

- Which organizations can sponsor a 457(b) plan?
- Why have a 457(b) plan?
- Who can participate in 457(b) plan?
- How 457(b) plans work with other plans
- Contribution types and limits
- “Special” 457(b) provisions



# Why 457 Plans?

- Used for certain governmental employers that are not permitted to sponsor a 403(b) or 401(k) plan.
- Used for tax-exempt employers due to concerns from Congress and the IRS that without the associated tax deduction, “excessive” income could be deferred when compared to for-profit counterparts.



# Types of 457 Plans

- Eligible 457(b) plans
- 457(f) (referred to as “ineligible”)
- LOSAP



# 457(b)

- What is a 457(b) plan?
  - An “eligible” plan
  - Two types
    - Governmental
    - Top Hat 457(b)



# Poll Question #1

Can a governmental employer sponsor both a 401(k) and a 457(b) plan?

A. Yes

B. No

# Background

	457(b) Governmental	457(b) Top Hat
<b>Tax Code Requirements</b>	<p>Must be a funded plan</p> <p>Trust, custodian, or annuity</p>	<p>Must be an unfunded plan (subject to creditors)</p> <p>May use a Rabbi Trust to provide limited protection</p>
<b>ERISA</b>	<p>Not subject to ERISA, by definition</p>	<p>To be exempt from certain ERISA rules (such as required funding), plan participation must be limited to a select group of management or highly compensated employees (HCEs)</p> <p>Note there is limited guidance – HCE is not necessarily the HCE definition for nondiscrimination testing</p>

# Eligible Sponsors

	457(b) Governmental	457(b) Top Hat
<b>Eligible Employers</b>	<p>A state or local government or agency or an instrumentality thereof</p> <p>Does not include Federal Government. For example, a Federal Credit Union (FCU) is not a governmental employer for this purpose.</p>	<p>Tax-exempt organizations. Generally, any tax-exempt organization may sponsor a 457(b) Top Hat plan (Not limited to 501(c)(3).)</p> <p>A “steeple” church is not an eligible sponsor. However, a “non-steeple” church may sponsor a Top Hat plan.</p> <p>Note – Until further guidance is issued, there are special transition rules that grandfather an FCU as a Top Hat plan if certain conditions are met</p>



# Eligible Employees

	457(b) Governmental	457(b) Top Hat
Eligible Employees	<p>All employees</p> <p>May include independent contractors</p>	<p>A select group of management or highly compensated employees</p> <p>May include independent contractors</p> <p>A non-steeple church is not required to limit participation; however, due to its unfunded status, it is recommended</p>

# Poll Question #2

For a 457(b) Top Hat plan, is there a specific definition of what constitutes a “select group?”

- A. Yes
- B. No



# Compensation Limit

	457(b) Governmental	457(b) Top Hat
<b>Maximum Compensation considered under §401(a)(17)</b>	As indexed:  2007 – \$225,000 2008 – \$230,000 2009 – \$245,000 2010 – \$245,000 2011 – \$245,000 2012 – \$250,000 2013 – \$255,000 2014 – \$260,000 2015 – \$265,000 2016 – \$265,000 2017 – \$270,000  Because of deferral limits, not usually an issue	Same

# Deferral of Compensation

	457(b) Governmental	457(b) Top Hat
<b>Types of contributions</b>	Pretax Elective Deferrals  Roth Deferrals (effective 2011)  Employer Contributions (treated as Employee Pretax Deferrals)	Pretax Elective Deferrals  No Roth Deferrals  Employer Contributions (treated as Employee Pretax Deferrals)

**Trap:** Employer contributions are treated as a deferral of income. Compensation is grossed up by the designated amount and then deferred. Thus, employer contributions count towards overall deferral limit and, if applicable to the employer, are subject to Federal Insurance Contributions Act (FICA) and Federal Unemployment Tax Act (FUTA) deductions

# Contribution Limits

	457(b) Governmental	457(b) Top Hat												
<b>Elective and Salary Deferral Limits</b>	Lesser of dollar limit as indexed or 100% of compensation	Same												
<b>Effective 2002: 457 contributions are no longer coordinated with 401(k) or 403(b) plans</b>	<table border="0"> <tr> <td>2007 – 2008</td> <td>\$15,500</td> </tr> <tr> <td>2009 – 2011</td> <td>\$16,500</td> </tr> <tr> <td>2012</td> <td>\$17,000</td> </tr> <tr> <td>2013 – 2014</td> <td>\$17,500</td> </tr> <tr> <td>2015 – 2017</td> <td>\$18,000</td> </tr> <tr> <td colspan="2">457(e)(15)</td> </tr> </table>	2007 – 2008	\$15,500	2009 – 2011	\$16,500	2012	\$17,000	2013 – 2014	\$17,500	2015 – 2017	\$18,000	457(e)(15)		Same
2007 – 2008	\$15,500													
2009 – 2011	\$16,500													
2012	\$17,000													
2013 – 2014	\$17,500													
2015 – 2017	\$18,000													
457(e)(15)														

# Age 50 Catch-Up

	457(b) Governmental	457(b) Top Hat
<b>Age 50 or Older Catch-up Elections Permitted</b>	<p>Age 50 Catch-Up is available to participants who attain age 50 by the end of the calendar year</p> <p>2007 – 2008 = \$5,000 2009 – 2014 = \$5,500 2015 – 2017 = \$6,000</p>	<b>Not Available!</b>

# Special Catch-Up

	457(b) Governmental	457(b) Top Hat
<b>Increased Deferral Limits for certain employees (Special Catch-up)</b>	<p>In any of the 3 years prior to the year in which participant attains normal retirement age, as defined by the 457 plan document</p> <p>Catch-up is the lesser of</p> <ul style="list-style-type: none"><li>(1) The deferral limit in effect;</li><li>or</li><li>(2) The sum of underutilized deferrals</li></ul> <p>In determining underutilized deferrals, you may only consider years in which the participant was eligible to contribute to the plan. (§457(b)(3))</p>	Same

# Special Catch-Up: Example

	Year	Eligible Amount	Actual Amount	Underutilized Amount
<p>ABC Hospital began sponsoring a 457(b) plan in July of 2009.</p> <p>Casi, an employee of ABC Hospital, became eligible for the Top Hat plan in August of 2013.</p> <p>Casi is 62 years old.</p> <p>Plan defines Normal Retirement Age as Age 65.</p>	2011	\$0	\$0	\$0
	2012	\$0	\$0	\$0
	2013	\$17,500	\$15,000	\$2,500
	2014	\$17,500	\$15,000	\$2,500
	2015	\$18,000	\$15,000	\$3,000
	2016	\$18,000	\$15,000	\$3,000

**Total Underutilized Amount: \$11,000**

For 2017, Casi may fund an additional \$11,000. The additional catch-up is the lesser of \$18,000 (the current deferral limit) and \$11,000 (her underutilized amount).

Casi's contribution limit for 2017 is \$29,000.



# Special Catch-Up Coordination

	457(b) Governmental	457(b) Top Hat
<b>Coordination of Catch-up Elections</b>	<p>A participant may elect the greater of the Special Catch-up or Age 50 Catch-up.</p> <p>Unlike 403(b) plans, the participant may <b>not</b> do both catch-ups.</p> <p>The 457(b) Age 50 Catch-up is not coordinated with 403(b) or 401(k) catch-up, so participant can do both.</p>	Not Applicable – only special catch-up available

**Trap:** The underutilized amount calculation can be difficult. As noted, only years when the plan was in place and the participant was eligible are considered. Prior to 2002, the coordination between 403(b) and 401(k) plans must be recognized.

# Poll Question #3

For those of you who administer/handle 457(b) plans – do you recommend having the special catch-up provision in the plan?

A. Yes

B. No



# Roth Contributions

	457(b) Governmental	457(b) Top Hat
<b>Roth Contributions and Conversations</b>	<p>Roth Contributions became available to 457(b) governmental plans on January 1, 2011</p> <p>In-plan Roth Rollovers or Roth Conversations are also available</p>	<b>Not Available!</b>



# Vesting

	457(b) Governmental	457(b) Top Hat
Can employer use a vesting schedule for Employer Contributions?	<p>Yes – Contributions count for limitation purposes in the year they vest.</p> <p>Can cause withholding issues if employee is subject to FICA</p> <p>Not recommended</p>	Same

**Trap:** If employer funds \$5,000 per year for 5 years and uses a 5 year cliff vesting schedule then the employee may have an excess deferral of \$7,000 if the amounts vest in 2017. (\$25,000 vs \$18,000). Vesting is not recommended.

**Trap:** If FICA/FUTA is not paid when contributed, the amount taxed when it is no longer subject to forfeiture will include the earnings (not just the contributions).

# Plan Compliance

	457(b) Governmental	457(b) Top Hat
<b>Top-Heavy Testing</b>	No	No
<b>ADP/ACP Test under §401(k)/(m)</b>	No	No
<b>§410(b) Coverage</b>	No	No
<b>5500 Reporting</b>	No	One time, initial filing only May file 5500 or alternative format
<b>Plan Documents</b>	Yes – subject to a written plan Note – individual states may have specific requirements	Yes – subject to a written plan
<b>ERISA Disclosures (SPDs etc.)</b>	No	No

# Poll Question #4

May the sponsor of a 457(b) plan use the Employee Plans Compliance Resolution System (EPCRS) to fix certain problems/errors?

- A. Yes
- B. No



# Loans and Distributions

	457(b) Governmental	457(b) Top Hat
<b>Loans</b>	Yes	No
<b>Commencement of Distributions</b>	Subject to the terms of the plan document; generally immediately following attainment of a distributable event	Subject to the terms of the plan document; generally on or after 90 days following attainment of a distributable event  This window is necessary for taxation purpose
<b>Distributable Events</b>	Subject to terms of plan document: <ul style="list-style-type: none"> <li>• Calendar year employee attains <b><u>age 70½</u></b></li> <li>• Severance from employment</li> <li>• Unforeseeable emergency</li> <li>• Small account distribution</li> </ul>	Same

**Trap:** 59½ is not a distributable event. The equivalent in a 457(b) plan is age 70½. Normal Retirement Age is not a distributable event – only affects catch-up limit.

# Distributions

	457(b) Governmental	457(b) Top Hat
<b>Required Minimum Distributions (RMDs) (§401(a)(9))</b>	Later of attainment of age 70 ½ or retirement May defer to April 1 following	Same
<b>In-Service Withdrawal (subject to plan provisions)</b>	<p>Distribution of Small Amounts</p> <p>The participant may elect (or the employer may direct) a distribution of small amounts while still employed if:</p> <ul style="list-style-type: none"> <li>• Total account balance does not exceed \$5,000</li> <li>• No deferrals have been made for the 2 years prior to distribution</li> <li>• No such prior distribution has occurred</li> </ul> <p>For Governmental Plans, rollovers can be ignored when determining total account balance</p>	Same



# Poll Question #5

Are the requirements and reasons for a 401(k) or 403(b) hardship versus a 457(b) plan unforeseeable emergency essentially the same?

- A. Yes
- B. No



# Unforeseeable Emergency

	457(b) Governmental	457(b) Top Hat
<b>Unforeseeable Emergency Withdrawals</b>	<p>Distribution may be made in the event of an unforeseeable emergency</p> <p>May include amounts necessary to pay federal, state or local income taxes (and penalties)</p>	Same

**Beware:** An unforeseeable emergency must truly be “unforeseeable.” The purchase of a residence or payment of college tuition are not considered “unforeseeable” under the regulations.

# Unforeseeable Emergency

	457(b) Governmental	457(b) Top Hat
<b>Unforeseeable Emergency Definition</b>	<p><b>An unforeseeable emergency is one that is...</b></p> <ul style="list-style-type: none"> <li>• An illness or accident of participant or beneficiary, participant's or beneficiary's spouse, participant's or beneficiary's dependent (as defined in Section 152(a))</li> <li>• A loss of participant's beneficiary's property due to casualty</li> <li>• Other similar extraordinary and unforeseeable circumstances arising as a result for events beyond the control of the participant or beneficiary</li> </ul>	Same

# Unforeseeable Emergency

	457(b) Governmental	457(b) Top Hat
<p><b>Unforeseeable Emergency –</b></p> <p><b>Example of “other circumstances or event”</b></p>	<ul style="list-style-type: none"> <li>• Imminent foreclosure of or eviction from the participant’s or beneficiary’s principal residence</li> <li>• Need to pay for medical expenses, including non-refundable deductibles, cost of prescription drugs/medication</li> <li>• Need to pay for funeral expenses of a spouse or a dependent (as defined in Section 152(a))</li> </ul>	<p>Same</p>

# Unforeseeable Emergency

	457(b) Governmental	457(b) Top Hat
<b>Unforeseeable Emergency – Satisfaction Test</b>	<p><b>Satisfaction Test:</b> The need can not be satisfied by any other resources including:</p> <ul style="list-style-type: none"> <li>• Reimbursement or compensation from insurance</li> <li>• Liquidation of the participant’s assets, to the extent the liquidation would not cause severe financial hardship</li> <li>• Cessation of deferrals under the plan</li> </ul>	<p>Same</p>

# Taxation

	457(b) Governmental	457(b) Top Hat
<b>When amounts are taxable</b>	At the time the money is received by the participant	When it is considered to have been made currently available  Currently available means the participant can request a distribution other than unforeseeable emergency or small account distribution
<b>Can a participant defer taxation?</b>	N/A – not taxed until distributed	Participants can defer current available (taxation) by completing an irrevocable election.  One additional election can be made which does not accelerate timing or amount of distribution(s).

# Tax Reporting

	457(b) Governmental	457(b) Top Hat
<b>Tax reporting on distributions</b>	<p>Form 1099-R</p> <p>Direct Payment of Certain Insurance available to “eligible retired public safety officers.” Up to \$3,000 per year is <u>tax-free</u>.</p> <p>Distribution may be eligible for tax-free rollover</p>	<p>W-2</p> <p>Exception for death benefits</p>
<b>Premature Distribution Penalty</b>	<p>The Section 72(t) 10% premature distribution penalty rules apply only to amounts rolled over from a <b>non-457</b> plan (assuming no 72(t) exception)</p> <p>Example: A rollover from a 403(b) plan may be subject to the premature distribution penalty if an exemption is not applicable</p>	<p>Not Applicable</p>

# Withholdings

	457(b) Governmental	457(b) Top Hat
<b>Income Tax Withholdings</b>	<p>Mandatory 20% withholding for income tax on distributions eligible for direct rollover</p> <p>Voluntary withholdings on distributions not eligible for rollover (10% default but can opt out)</p> <p>Voluntary withholdings on Roth Rollover Conversions</p>	<p>Default 25% withholding applies if participant does not complete a Form W-4 or equivalent</p> <p>Participant may file Form W-4 or equivalent to specify the number of exemptions or to add/adjust withholdings</p>



# Rollovers

	457(b) Governmental	457(b) Top Hat
<b>Direct Rollovers to other qualified plan/IRA</b>	<p>Yes – May roll over to another eligible 457(b) governmental, 401 or 403(b) plan, or IRA</p> <p>Participant must have a distributable event in order for a rollover to occur</p> <p>Who: The participant or a spousal beneficiary in the event of participant’s death</p> <p>Who: A non-spousal beneficiary may roll over a death benefit to an inherited IRA only (made available by PPA)</p> <p>RMDs, hardship distributions and payments spread over ten years or more are not eligible for rollover</p>	<p>Distributions from a 457(b) Top Hat plan may <b>NOT</b> be rolled over to another plan.</p> <p>A terminated participant may transfer to another eligible 457(b) Top Hat plan if:</p> <ul style="list-style-type: none"> <li>• It’s permitted by both distributing plan and recipient plan</li> <li>• The participant is eligible to participate in the recipient’s plan</li> <li>• Any prior irrevocable election is maintained</li> </ul>

# Poll Question #6

If an account from a 457(b) governmental plan is rolled over to a 401(k) or 403(b) plan, does the 457(b) plan account balance “retain” the exemption from the ten-percent penalty?

A. Yes

B. No



# Transfers

	457(b) Governmental	457(b) Top Hat
Non-taxable Transfers	<p>Direct transfer to purchase service credits in a governmental defined benefit plan</p> <p>Transfer between any 457(b) governmental plans of the same employer</p> <p>Post-severance transfers from one 457(b) governmental plan to another employer's 457(b) governmental plan</p> <p>Transfers do not require tax reporting</p>	<p>Transfer between plans of the same employer (No specific guidance allows this)</p> <p>Post-severance transfers from one 457(b) tax-exempt plan to another 457(b) tax-exempt plan</p> <p>Transfers must continue to recognize any irrevocable election made in prior plan.</p>

# 457(f)

	457(f) Governmental	457(f) Top Hat
<b>Ineligible 457(f) plans</b>	<p>Plans that are not eligible 457(f) plans and are not otherwise described in Section 457 are “ineligible” plans</p> <p>Amounts subject to 457(f) are <b>taxable when no longer subject to a substantial risk of forfeiture</b> (vesting)</p> <p>A substantial risk of forfeiture implies there is an expectation of future service</p> <p>Amounts contributed to a 457(f) plan are usually employer-funded</p> <p>Amounts contributed by the employer are considered a deferral of income. Amounts are subject to FICA/FUTA when vested.</p>	Same

# LOSAP

## Length of Service Award Program (LOSAP)

LOSAP is a plan paying length of service awards to bona fide volunteers (and their beneficiaries) on account of qualified services.

“Qualified services” means fire fighting and prevention services, emergency medical services, and ambulance services.

Employer contribution only. Maximum annual contribution is \$3,000. No rollovers or loans are permitted.

Section 457(e)(11)(A)(ii)

# Frequently Asked Questions (FAQs)

- Are 457(b) limits aggregated with 403(b) limits?
  - No
- Can a 457(b) plan terminate?
  - Yes
- Can a 457(b) plan consist of employer contributions only?
  - Yes, but they're still treated as a deferral of income
- Can a Top Hat 457(b) plan allow age 50 catch-ups?
  - NO!

# Plan Design Options/Multiple Plans

- Governmental Employer
  - 401(a) plan
    - 401(k) – if grandfathered
    - 414(h) pickup plan
  - 457(b) Governmental plan
  - 457(f) Top Hat plan
- Non-Profit Employer
  - 403(b) plan
  - 401(k) plan
  - 457(b) Top Hat plan
  - 457(f) Top Hat plan



Please note: This list does not include all plan options available. In addition, certain states may have restrictions on governmental plan options.

# Plan Design Options/Multiple Plans

## Best” Retirement Programs to Maximize Benefits

- Governmental Employer
  - 457(b) Governmental plan (deferral only plan)
  - 401(a) plan (employer match and/or non-elective contributions)
    - This may also be the best option for “NQ”/executive benefits.
- Non-Profit Employer
  - 403(b) plan
  - 457(b) Top Hat plan (select group)
  - 457(f) Top Hat plan (a few keys executives from select group)



# Questions?